IN THE HIGH COURT OF JUDICATURE AT MADRAS

DATED : 01.11.2006

Coram :

THE HONOURABLE MR.JUSTICE R.BALASUBRAMANIAN
AND
THE HONOURABLE MR.JUSTICE P.P.S.JANARTHANA RAJA

Tax Case (Appeal) No.134 of 2003

Commissioner of Income Tax,
Salem. ..Appellant

Vs

B.Desraj ..Respondent

Appeal under Section 260A of the Income Tax Act, 1961 against the order of the Income Tax Appellate Tribunal, Madras, 'A' Bench dated 06.02.2003 in I.T.A. No.2320/Mds/94 for the assessment year 1991-92. against the order dated 22.08.1994 in I.T. Appeal No. 349-C/94-95 on the file of the Commissioner of Income (Appeals) Coimbatore against the order dated 23.03.1994 and amde in PAN/GIR NO. Ward- I (7) Salem - 7 on the file of the Income Tax Officer W-I (7) Salem - 7.

For Appellant : Mr.J.Naresh Kumar

For Respondent : Mr.V.S.Jayakumar for
Mr.V.D.Gopal

JUDGMENT

P.P.S.Janarthana Raja, J.

This appeal is filed under Section 260A of the Income Tax Act, 1961 by the Revenue against the order of the Income Tax Appellate Tribunal, Madras, 'A' Bench dated 06.02.2003 passed in I.T.A. No.2320/Mds/94. On 15.10.2003, this Court admitted the appeal and formulated the following substantial question of law.

"Whether in the facts and circumstances of the case the Tribunal was right in holding that the deduction under section 80HHC in respect of the duty drawback and the cash compensatory support is allowable even though no export was done by the assessee?"

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2. The facts leading to the above substantial question of law are as under:

The assessee is an 100% Export Oriented Unit. The relevant assessment year is 1991-92 and the corresponding accounting year ended on 31.03.1991. The assessee filed Return of income on 30.11.1992 admitting a total income of Rs.1,50,860/-. The Return was processed under Section 143(1)(a) of the Income-tax Act (hereinafter referred to as the "Act"), after making prima facie adjustment and rejecting the assessee's claim of deduction under Section 80HHC of the Act. Later, assessment was taken up for scrutiny and the assessment was completed under Section 143 (3) of the Act determining a total income of Rs.9,27,500/-. While completing the assessment, the Assessing Officer was of the view that the assessee is not entitled to deduction under Section 80HHC of the Act, on the ground that there was no export during the year. Aggrieved by the order, the assessee filed an appeal to the Commissioner of Income-tax (Appeals). The C.I.T. (A) allowed the appeal and set aside the order of the lower authority. Aggrieved, the Revenue filed an appeal to the Income-tax Appellate Tribunal (hereinafter referred to as the "Tribunal"). The Tribunal dismissed the Revenue's appeal and confirmed the order of the C.I.T.(A).

3. Learned Standing Counsel appearing for the Revenue submitted that the assessee had not done any export and therefore, the assessee is not entitled for deduction. He further submitted that on a mere receipt of the duty drawback and cash compensatory support during the accounting year does not entitle the assessee for deduction as there was no export made by the assessee during the accounting year. Further it is submitted that the amounts received could not be considered as profit derived from export. He relied on the Supreme Court judgment reported in 237 ITR 579, in the case of Commissioner of Income-tax Vs. Sterling Foods.

4. Learned counsel appearing for the assessee submitted that the assessee is an 100% export unit. During the relevant year of account, the assessee received the cash compensatory support to the tune of Rs.7,74,868/- and duty drawback amount of Rs.34,565/- for the export made during the year ending 31.03.1990, relevant to the assessment year 1990-91. During the year under consideration, the assessee was right in claiming deduction under Section 80HHC of the Act in respect of the incentive amounts pertaining to duty drawback and cash compensatory support, actually received during the year, as it is connected with the export transaction only. He further submitted that cash compensatory support as well as duty drawback were granted to the assessee only because of the export

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made and hence it is a profit derived from export. The learned counsel also contended that the said incentives received earlier to which export was made, are certainly entitled to relief and because of the belated receipt of the incentives, the assessee could not be denied the benefit. It is also further submitted that Section 80HHC of the Act is to provide certain incentive to export houses and hence, the exempted provisions are to be construed liberally. He also relied on the Supreme Court judgment reported in 284 ITR 548 in the case of P.R.Prabhakar Vs. Commissioner of Income-tax to support his contention.

5. Heard the counsel. During the year ended 31.03.1990, the assessee did export business for a turnover of Rs.38,72,885/- and a profit to the tune of Rs.37,583/- was earned. The relevant assessment year in the present case is 1991-92 and during the year, the assessee not made any export, but received cash compensatory support to the tune of Rs.7,74,868/- and duty drawback of Rs.34,565/-. Eventhough the said amounts are relating to the export made in the immediate preceding year, the Central Government quantified the incentive amounts later and the quantified amounts were received by the assessee only during the year. The assessee is following the cash system and hence the incentive amounts received, was treated as income on receipt basis during the assessment year. The undisputed fact is that the assessee has not made any export during the relevant assessment year 1991-92. Because of the amendment of Section 28 of the Act, by the Finance Act, 1990 by inserting Clauses (iiia) (iiib) and (iiic) with retrospective effect with a view to ensure that cash compensatory support, duty drawback and profit on sale of import entitlement licenses shall be taxable under the head "Profits and gains of business or profession", the said amounts received could not be considered as export profit. Section 80HHC of the Act deals with granting deduction, which reads as under:

"80HHC. Deduction in respect of profits retained for export business. -

(1) Where an assessee, being an Indian company or a person (other than a company) resident in India, is engaged in the business of export out of India of any goods or merchandise to which this section applies, there shall, in accordance with and subject to the provisions of this section, be allowed, in computing the total income of the assessee, a deduction of the profits derived by the assessee from the export of such goods or merchandise:

....

(1A) ....

(2)(a) This section applies to all goods or merchandise, other than those specified in clause (b), if the sale proceeds of such goods or merchandise exported out of India are received in, or brought into, India by the assessee (other than the supporting manufacturer) in convertible foreign exchange, within a period of six months from the end of the previous year, or, where the

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Chief Commissioner or Commissioner is satisfied (for reasons to be recorded in writing) that the assessee is, for reasons beyond his control, unable to do so within the said period of six months, within such further period as the Chief Commissioner or Commissioner may allow in this behalf.
(b) ....
(3) For the purposes of sub-section(1), profits derived from the export of goods or merchandise out of India shall be the amount which bears to the profits of the business (as computed under the head "Profits and gains of business or profession"), the same proportion as the export turnover bears to the total turnover of the business carried on by the assessee."

Under Section 80HHC of the Act, where an assessee, being an Indian company or a person (other than a company) resident in India, is engaged in the business of export out of India of any goods or merchandise to which this section applies, there shall, in accordance with and subject to the provisions of this section, be allowed, in computing the total income of the assessee, a deduction of the profits derived by the assessee from the export of such goods or merchandise. A tax concession was given under Section 80HHC of the Act, in order to compensate the exporter for the comparative disadvantage faced by him in the international market. As in this case, what we have to see is, whether there is a profit derived by the assessee from the export business or not. The undisputed fact is that, during the relevant year of account, the assessee received cash compensatory support to the tune of Rs.7,74,868/- and duty drawback of Rs.34,565/- for the export made in the immediate preceding year. The said two amounts could not be considered as profits derived by the assessee from the export business. The Supreme Court in the case of Commissioner of Income-tax Vs. Sterling Foods reported in 237 ITR 579, held as follows:

"We do not think that the source of the import entitlements can be said to be the industrial undertaking of the assessee. The source of the import entitlements can, in the circumstances, only be said to be the Export Promotion Scheme of the Central Government whereunder the export entitlements become available. There must be, for the application of the words "derived from", a direct nexus between the profits and gains and the industrial undertaking. In the instant case, the nexus is not direct but only incidental. The industrial undertaking exports processed sea food. By reason of such export, the Export Promotion Scheme applies. Thereunder, the assessee is entitled to import entitlements, which it can sell. The sale consideration therefrom cannot, in our view, be held to constitute a profit and gain derived from the assessee's industrial undertaking."

Following the above Supreme Court judgment, it is evident that the cash compensatory support and duty drawback amounts could

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not be held as profits derived from export. Sub-section (3) of Section 80HHC of the Act, deals with the formula for computing the profit derived from the export of goods for the purpose of sub-section (1) of the Act. The formula is as under:

$$\text{Profit of the business (including export incentives)} \times \frac{\text{Export turnover (sale proceeds actually received in foreign exchange}}{\text{Total turnover (excluding export incentives).}}$$

In the present case, the export turnover and the total turnover during the year ended 31.03.1991 are nil and therefore, the assessee is not entitled to deduction under Section 80HHC of the Act. Further it is seen that the wording mentioned in the section is "profits derived by the assessee from the export of such goods or merchandise". The expression used in the Section is "derived from". Whenever the said expression is used, the Legislature wanted to give a restricted meaning. If the expression "attributable to" is used, it means the Legislature wanted to give wider meaning, than the expression "derived from". If the expression "attributable to" is used, the intention is to cover receipts from sources other than actual conduct. Here, the expression used is "derived from" and hence, we have to give restricted meaning only. Hence, there should be direct nexus between profit and export. These incentives could not be profit derived from the export business, because it is given only after export by the Government of India as incentives to the exporter. The cumulative effect of the following factors, namely -

a) No export made during the year;
b) Only incentives are received during the year;
c) The said incentives are not profit derived from export;
d) Non-compliance of the formula, as contemplated under Section 80HHC(3) of the Act,

will certainly disentitle the assessee to claim relief under Section 80HHC of the Act. The other argument of the assessee is, if the assessee follows mercantile system of accounting, these incentives will go into the computation for the purpose of relief under Section 80HHC of the Act. Because the assessee is following the cash system, Revenue denied the benefit on the sole ground that there was no export during the year. Mere receiving incentives during the year alone will not entitle the assessee to relief under Section 80HHC of the Act. It is evident from the fact that the assessee is still in the export business, but there was no actual export during the year. Merely continuing the business is not sufficient to get the benefit provided under Section 80HHC of the Act, unless there is

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actual export made during the year.

6. In the case of P.R.Prabhakar Vs. Commissioner of Income-tax (SC), cited supra, the assessee carried on business of export of his own products and also procured export contracts for other exporters on commission. He derived income of Rs.56,69,321/- by way of commission, whereas as an exporter of goods, he incurred a loss of Rs.6,372/-. The value of the total exported goods outside India, by the assessee, during the relevant assessment year was Rs.3,67,600/-. The assessee claimed deduction under Section 80HHC of the Act. The said exemption claimed was disallowed by the Assessing Officer on the ground that the assessee had incurred loss in respect the export business. Aggrieved by the same, the assessee filed an appeal before the Commissioner of Income-tax (Appeals) and the same was dismissed. Aggrieved, the assessee filed appeal before the Income-tax Appellate Tribunal. The Income-tax Appellate Tribunal was of the view that the commission received from other exporters has to be taken into consideration in computing the relief under Section 80HHC of the Act. Aggrieved by the order, the Revenue filed an appeal before the High Court and the High Court reversed the order of the Tribunal. Aggrieved, the assessee took up the matter to the Supreme Court. The Supreme Court reversed the order of the High Court and held that the earning of commission, being part of the export business, the income derived therefrom also to be taken into consideration for granting relief under Section 80HHC of the Act. Because of the loss as exporter of goods, the assessee should not be denied exemption under Section 80HHC of the Act. The distinct factor in the Supreme Court judgment is, there was export by the assessee during the year. But, in the present case, the facts are different, because there was no export during the year. Hence, the Supreme Court judgment is distinguishable and hence it will not help the assessee's case.

7. In the case of Sanjeev Malhotra Vs. Commissioner of Income-tax, reported in 286 ITR 364, the Delhi High Court considered the scope of Section 80HHC of the Income-tax Act and held that there should be actual export during the year for the purpose of availing benefit under Section 80HHC of the Act. In that case, the assessment year was 1998-99 and the assessee filed Return declaring an income of Rs.11,56,780/- after claiming deduction of Rs.31,97,357/- under Section 80HHC of the Act. The assessee had, for that year, shown export sales of Rs.24,822/- and profit on sale of import entitlements of Rs.35,46,150/-. The Assessing Officer came to the conclusion that no exports had been made by the assessee and also found that the import entitlements sold by the assessee related to exports made in the assessment year 1995-96. As regards the export sale of Rs.24,822/- the Assessing Officer held that the same represented the price of gift samples and not trade samples as contended by the assessee. Hence, there was no export sale during the year under

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consideration and the Assessing Officer disallowed the claim. Aggrieved by the order, the assessee filed an appeal to the C.I.T.(A), who confirmed the said order. The assessee took further appeal before the Tribunal and the Tribunal also held that no deduction under Section 80HHC was permissible unless there was actual export in the year under consideration. Against that, the assessee filed an appeal to the High Court and the High Court also confirmed the order of the Tribunal and was of the view that the export of goods was a condition precedent for claiming deduction under Section 80HHC of the Act. We also agree with the view taken by the Delhi High Court that, for the purpose of claiming deduction under Section 80HHC of the Act, there should be actual export during the year.

8. In view of the foregoing reasons, we are of the view that mere receipt of amounts for duty drawback and cash compensatory support during the accounting year, does not entitle the assessee for deduction under Section 80HHC of the Act, as the assessee had not made any export during the accounting year. Under these circumstances, we answer the question in favour of the Revenue and against the assessee. No costs.

km

Sd/

Asst.Registrar

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Sub Asst.Registrar

To

1. THE ASSISTANT REGISTRAR
INCOME TAX APPELLATE TRIBUNAL
RAJAJI BHAVAN
III FLOOR BESANT NAGAR
CHENNAI 90

2. THE INCOME TAX APPELLATE
TRIBUNAL MADRAS A BENCH
MADRAS

3. THE COMMISSIONER OF INCOME
TAX, SALEM

4. THE COMMISSIONER OF INCOME
TAX, (APPEALS) COIMBATORE

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5. THE INCOME TAX OFFICER
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(7) SALEM 7

+ one cc to Mr. V.S. Jayakumar, Advocate sr no. 51393
+ one cc to Mr. N. Muralikumaran, Advocate sr no. 51644

GM(Co)
NM(20.11.2006)

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